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C O N F I D E N T I A L SECTION 01 OF 03 LJUBLJANA 000378

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TAGS: ECON EINV ETRD SI
SUBJECT: THE PRIVATIZATION TWO STEP: UPDATE FROM SLOVENIA

REF: A. LJUBLJANA 0132

¶B. 05 LJUBLJANA 0766
¶C. 05 LJUBLJANA 0546
¶D. 05 LJUBLJANA 0489

Classified By: COM Thomas B. Robertson, reasons 1.4(b) and (d)

¶1. (C) Summary: The Government of Slovenia (GOS) has announced it will soon begin privatizing two of its significant assets: telecommunications operator Telekom Slovenije; and the country's second largest financial institution, Nova Kreditna Banka Maribor (NKBM). Though somewhat ill-timed coming on the heels of the failed further privatization of Slovenia's largest bank, Nova Ljubljanska Banka (NLB), at first glance this move is encouraging. The government of Prime Minister Janez Jansa came to power promising to act on privatization. Preparations for doing so, however, have taken longer than expected. Indeed, there are growing concerns that despite the stated GOS commitment to privatization, with the smoothly growing economy and broad public skepticism about selling prime Slovenian business assets to foreigners, the political costs of privatization may be too high. If that is the case, the privatizations of NKBM and Telekom could end up following the model of previous impotent efforts by past Slovenian governments to extract the state from its influential role in the economy. End summary.

NLB

¶2. (C) As reported in March 2006 (ref A), Finance Minister Andrej Bajuk told COM that his plan for privatization was for the GOS to maintain no more than a "golden share" of state ownership (presumably 25 percent or less), and only in certain key industries. It is unclear, however, how Bajuk intends to implement this model in the case of NLB. In mid-May, long-term investor in NLB, Belgian bank KBC, announced that it would "reconsider" its ownership role in the bank. KBC, a 34% owner of NLB, said that it intends to move from the role of a strategic investor to a financial one, indicating a decrease in a long term role in Slovenia.

¶3. (C) Since the purchase of its initial, minority stake in NLB, KBC had long made clear its interest in becoming the majority owner. In recent weeks, when it became clear that the GOS was unwilling to allow KBC to take over NLB, the Belgians conceded and offered to increase their stake to only

49% on the condition of receiving effective management control. The GOS rejected this offer also, at which point KBC decided to change its relationship with NLB. As Post understands it, Belgian management board members of NLB have resigned and KBC is interested in selling its stake. Contacts tell Econoff that despite Bajuk's stated preference for only a "golden share," selling a controlling interest in Slovenia's most important financial institution was a politically untenable proposal.

NKBM

¶4. (SBU) Long-promised but never executed, the GOS's recent announcement to privatize NKBM could be the first step in Bajuk's much touted plan to build a "second financial pillar" around NKBM to provide a competitive and compelling alternative to NLB. In mid-May, the GOS announced that it intended to privatize NKBM in two phases. In the first phase, 20% of the bank will be offered for sale to a strategic investor through an international public tender. (Note: The GOS, in its announcement, failed to define "strategic investor." End Note.) Another 5-10% will be offered to Slovene citizens, and a further 20-25% will be sold to institutional investors in a public tender. At the end of phase one, the government will retain a 51% share. In phase two, the GOS will pare down its holdings to 25% by selling the balance to institutional investors.

¶5. (C) The Jansa government has made previous attempts to sell off its stake in NKBM. These attempts failed, however, largely due to overpriced offerings and NKBM's lack of reach beyond Slovenia reducing its attractiveness (ref D). The

government has not been forthcoming about a pricing strategy but has indicated a 24 month timeframe to complete the process. Even baby steps towards privatization of NKBM are welcome given that the GOS declared its intention to do so more than 18 months ago. What remains unclear, however, is whether the government will be able to find a partner interested in purchasing a bank with less than half the market share of NLB, no foreign operations, and limited presence outside of northeast Slovenia. Moreover, in light of KBC's difficulties in obtaining a majority stake in NLB, the GOS may have difficulty finding a foreign investor willing to buy a minority share of the number two banking institution at a price that makes financial sense.

Telekom Slovenije

¶6. (SBU) On the same day it announced plans to move forward with privatizing NKBM, the GOS also prsented its strategy for the privatization of Telekom Slovenije and its subsidiary companies, cellular provider Mobitel and ISP SiOL. In the first phase (planned for Fall 2006), 5% of Telekom's stock will be listed on the Ljubljana Stock Exchange. The price at which the stock trades will be the valuation used to offer an approximate 40% stake in the company to a strategic partner to be chosen through an international tender (although the timeline for this has yet to be finalized). The GOS intends to retain a stake in Telekom of 25% plus one share. Post understands that any potential strategic partner will be required to submit a development plan for Telekom and that the owner must hold the shares it purchases directly, not through a subsidiary. Another key requirement would be that the partner retain existing equipment sourcing relationships that Telekom Slovenije has with Slovene suppliers.

¶7. (SBU) One of the largest business entities in Slovenia, the sale of Telekom Slovenije has the potential to generate significant revenue for the GOS. It is unclear, however, whether the sale of the company in its entirety will be

sufficiently attractive to a foreign investor. Some observers have noted that Telekom subsidiary Mobitel has far greater growth prospects and therefore a potentially higher valuation as a separate entity. Attached as one piece of the parent company, some would argue, makes Mobitel less attractive. Still other pundits note, however, that while the optimal time for sale of a fixed-line phone company may have passed, Telekom's infrastructure and cash-generating potential will attract interest from high quality investors.

Comment

¶8. (C) The announced privatizations of both Telekom and NKBM are, on the surface, welcome. The Jansa government has taken steps to privatize these businesses where governments in the past have not even tried. Despite the announced privatization plans, however, the current GOS has made little progress on its economic reform agenda. In office over 18 months, there has been almost no measurable progress on privatization or any other area of economic reform, key elements of the campaign platform on which this government was elected. The only privatization that has occured, the sale of retailer Mercator by state-owned funds to other state-controlled businesses was, at best, dubious in nature (ref B). Moreover, the GOS has yet to show any real difference from previous coalitions who also announced, but never followed through on, plans to extract the state from its ownership role in a wide swath of Slovene businesses.

¶9. (C) Slovenes often note that the privatization process of domestic companies began in the late 1980s, as shares in companies that were "socially owned" by citizens of Yugoslavia were distributed to employees, managers, and the general populace at values that were often well below the intrinsic value of the firms assets. The state-owned funds that were set up to distribute these shares, KAD and SOD, are still two of the larger owners of Slovene companies today. At the time of Slovenia's independence, there was little interest in allowing foreigners to participate in the privatization of the country's successful enterprises, as for

the first time in its history, Slovenia was a truly independent nation. This resistance to foreign ownership continues today, with Slovenia having one of the lowest levels of foreign direct investment in Europe. As an EU member state, though, the GOS realizes that any privatization process will almost certainly have to be done through an international tender, risking takeover of domestic entities by foreign firms.

¶10. (C) In light of the failure to move forward on further sale of NLB to a significant owner, pundits and outside observers question the feasibility and seriousness of the GOS in its stated plans for NKBM and Telekom. There is little indication in any of the privatization plans that the GOS truly intends to remove itself from a position of influence. Rather, the view of some contacts is that the GOS hopes to cash-in through these sales without really giving up a significant amount of control.

¶11. (C) The links between the state and the business sector are as strong in the current center-right government as they were in center-left governments of the past. With the replacement of the management of nearly all state-owned businesses since the election of the Jansa government in October 2004 (ref C), lack of movement on privatization seems to indicate that the current GOS is no more inclined than its predecessors to decrease the role of the state in the business sector now that it has the power to steer the economy in the manner it sees fit. Moreover, the current GOS appears unwilling to take the political risk of selling off part or all of its stakes in companies that are often seen as the crown jewels of Slovenia. In addition to fear of

takeovers by foreigners, successful, if not robust, economic growth causes many Slovenes to wonder why change is necessary. Serious steps toward improving the operation of state-owned businesses by sales to those more inclined and trained to run them in the most efficient manner possible could well be a long time in coming. End comment.
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